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## **INTRODUCTION**

In accordance with the City Auditor's 1989-90 Audit Workplan, we have reviewed the City of San Jose's franchise agreement with Heritage Cablevision, Inc. We conducted our audit in accordance with generally accepted government auditing standards, and limited our work to those areas specified in the Scope and Methodology Section of this report.

## **BACKGROUND**

### **Rules And Regulations**

The San Jose Municipal Code (Chapter 15.28), the City Charter (Article XIII) and the City Ordinance (No. 22128) prescribe the City's rules and regulations governing cable television franchises. Some of the requirements of the ordinance include system expansion, service level, educational, municipal and community access, subscriber complaint procedures, and franchise fee payments.

### **History**

In 1965, the City of San Jose entered into a franchise agreement with Gillcable Industries, Inc. to provide cable television services. Although the agreement did not expire until 1990, Gillcable approached the City in 1980 with a request for an extension. Tentative agreement was reached in 1983, but negotiations broke down over a franchise fee dispute.

In 1984, the United States Congress passed the Cable Communications Policy Act of 1984 which allows cities to impose franchise fees of up to five percent. In December 1985, Gillcable and the City agreed to raise the franchise fee from two percent to three percent until December 31, 1990 and then to five percent thereafter. The December 1985 agreement also changed the definition of the revenues that were subject to franchise fees from the "Basic 24 Channel Service" to all gross revenue derived from subscription payments. In 1987, a disagreement ensued between the City and Gillcable as to whether or not community access operating expenses

were deductible from franchise fees payable to the City. The City demanded that Gillcable pay an additional franchise fee of \$209,704. In November 1987, Gillcable and the City settled for \$100,000. In March 1988, Gillcable sold its controlling stock interest in the San Jose cable franchise to Heritage Cablevision and the company was subsequently renamed Heritage Cablevision.

### **Revenue**

From 1985-86 to 1988-89, the City's franchise fees from cable television have increased more than 2.5 times. TABLE I summarizes cable television franchise fees for 1985-86 through 1988-89.

**TABLE I**  
**SAN JOSE CABLE TV FRANCHISE FEES**  
**FROM 1985-86 TO 1988-89**

1985-86	\$ 426,349
1986-87	586,823
1987-88	1,094,504
1988-89	<u>\$1,125,133</u>
Total	<u>\$3,232,809</u>

These large increases in cable television franchise fees are primarily due to the following:

1. Since 1984, the basic rate charged to cable customers has increased from \$15.95 to \$20.95.
2. Gillcable increased the number of units served by installing cable in existing neighborhoods. According to Gillcable, all existing

neighborhoods have been served and any increase in business will come from future residential developments.

3. The December 1985 agreement between Gillcable and the City increased the franchise fee from two percent to three percent and expanded the types of revenues subject to the fee.

## **Scope and Methodology**

Our audit objectives were to determine 1) if Heritage Cablevision, Inc. has complied with the reporting and payment provisions of its franchise agreement with the City, and 2) whether the franchise fees the City is receiving are for the correct amount and remitted in a timely manner. We also reviewed for effectiveness and efficiency, the City's receiving and monitoring of franchise fee payments. Our methodology included reviewing 1) applicable City Charter, Code, and Ordinance provisions, 2) the adequacy of Heritage Cablevision's procedures for recording and reporting gross revenues, and 3) the propriety of franchise fee payments made to the City. Our review covered the period of May 1, 1988 to November 30, 1989. We also interviewed City staff and members of the City Attorney's Office.

## FINDING I

### **IMPROVEMENTS ARE NEEDED REGARDING THE CALCULATION, DOCUMENTATION, AND REVIEW OF CABLE TELEVISION FRANCHISE FEES**

The San Jose Municipal Code defines the City's and Heritage Cablevision's (Franchisee) rights and responsibilities regarding cable television service, charges and franchise fees. However, our review of franchise fee payments from May 1988 through November 1989 revealed that:

- ◆ The Franchisee did not adequately document why more than \$357,000 in franchise fees were not paid to the City.
- ◆ Absent additional Franchisee's justification, it appears that the City was underpaid an estimated \$175,000 in franchise fees.
- ◆ The Franchisee used unauthorized methodologies to calculate the City's franchise fee.
- ◆ The City only minimally monitors, reviews or verifies franchise fees.

As a result, the City is exposed to the risk of not receiving all of the cable television franchise fees to which it is entitled.

### **The San Jose Cable Television Franchise Fee Ordinance**

Section 15 of City Ordinance No. 22128 prescribes the rules and regulations governing the City's cable television franchise fee. The Ordinance defines what is and is not gross revenues for the purpose of calculating the City's franchise fee and states that "*The payment of franchise fees shall be in lieu of any utility users' or users tax.*" Thus, it is critical that the



Franchisee document and support any revenues and income that it excludes from its franchise fee computation.

**The Franchisee Did Not Document \$357,000  
In Franchise Fee Reductions**

For the period of May 1, 1988 through November 30, 1989, the Franchisee excluded about \$11,900,000 from its computation of franchise fees due to the City. As a result of these exclusions, the City's cable television franchise fee was reduced by \$357,000. However, our review revealed that the Franchisee cannot adequately document why these revenue items were excluded from its franchise fee computation.

Our review of the Franchisee's computerized accounts receivable system showed 161 types of services for customers in San Jose. The Franchisee excluded revenues from 70 of these 161 services from its computation of the City's franchise fee.<sup>1</sup> From January 1, 1989 through November 30, 1989, the Franchisee earned revenue of \$5,747,066 from those services excluded from the franchise fee computations. The Franchisee was unable to provide us with documentation for the earned revenues from the services excluded from the franchise fee computations for the period May 1, 1988 through December 31, 1988. However, we estimate those revenues to be \$4,104,000. TABLE II summarizes our estimate of revenues excluded from franchise fee computation from May 1, 1988 through November 30, 1989.

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<sup>1</sup> APPENDIX C-1 is a listing of the 70 services the Franchisee excluded from its franchise fee computations.

**TABLE II**

**SUMMARY OF SERVICE REVENUES EXCLUDED FROM  
FRANCHISE FEE COMPUTATIONS FROM  
MAY 1, 1988 THROUGH NOVEMBER 30, 1989**

Excluded Revenue Categories	<u>70</u>
Revenues Excluded From Franchise Fee Computations	
January 1, 1989 - November 30, 1989	\$5,747,066
Estimate for May 1, 1988 - December 31, 1988	<u>4,104,000</u>
TOTAL	<u>\$9,851,066</u>

In addition, the Franchisee excluded from franchise fee computations an additional \$2,049,644 in income for the period of May 1, 1988 through November 30, 1989. This income was shown on the Franchisee's monthly operating statements as income other than services but not recorded through the Franchisee's computerized accounts receivable system. TABLE III summarizes the \$2,049,644 in non-service income that the Franchisee excluded from fee computations from May 1, 1988 through November 30, 1989.

**TABLE III**  
**SUMMARY OF NON-SERVICE INCOME EXCLUDED**  
**FROM FEE COMPUTATIONS FROM**  
**MAY 1, 1988 THROUGH NOVEMBER 30, 1989**

1988	Channel		Classified	Agency	Other		Home	Cable
<u>Month</u>	<u>Lease</u>	<u>Advertising</u>	<u>Advertising</u>	<u>Discounts</u>	<u>Rent</u>	<u>Other</u>	<u>Shopping</u>	<u>Store</u>
May	8,275	15,380	13,178		6,517	43,166	13,160	697
June	4,500	8,500	14,357		3,677	44,914	13,272	931
July	3,725	8,500	16,303		5,177	43,502	14,559	567
August	4,100	8,500	16,683		4,677	47,482	14,824	248
September	2,625	8,500	46,905		4,177	47,036	13,027	804
October	950	26,225	33,300		4,177	49,199	8,763	460
November	1,975	10,000	30,112		4,177	50,840	16,746	498
December	650	19,896	36,666		4,177	54,233	19,152	1,103
1989								
January	2,075	10,000	37,060		4,177	60,268	18,632	438
February	2,475	37,108	39,172		6,612	60,434	7,918	405
March	675	10,000	37,032		4,647	53,984	14,380	152
April	1,200	10,000	35,538		4,612	51,257	15,183	331
May	2,600	10,000	38,195		4,612	50,904	11,970	335
June	1,000	10,000	42,060		4,612	53,856	12,943	495
July	1,000	10,000	45,164		4,612	<1,596>	16,154	515
August	1,000	25,532	51,313		4,923	774	16,570	488
September	495	0	44,832		4,463	1,793	15,775	255
October	1,745	15,518	42,694		4,647	3,874	21,320	450
November	<u>425</u>	<u>0</u>	<u>48,734</u>	<u>&lt;1,560&gt;</u>	<u>4,948</u>	<u>1,789</u>	<u>15,733</u>	<u>174</u>
TOTAL	<u>41,490</u>	<u>243,659</u>	<u>669,298</u>	<u>&lt;1,560&gt;</u>	<u>89,621</u>	<u>717,709</u>	<u>280,081</u>	<u>9,346</u>
GRAND TOTAL = <u>\$2,049,644</u>								

It should be noted that the Franchisee was unable to provide us with an analysis of the composition of the \$2,049,644 that was excluded from franchise fee computation. Thus, the Franchisee did not have adequate and available documentation for:

- Service Revenues that were excluded from franchise fee computations for the period May 1, 1988 through December 31, 1988	\$4,104,000	(Estimated)
- Non-Service Income excluded from fee computations from May 1, 1988 through November 30, 1989	<u>2,049,644</u>	
Total Undocumented Exclusions From Franchise Fee Computations	<u>\$6,153,644</u>	

In our opinion, the Franchisee's failure to maintain its records in a form that would enable City staff to understand the composition of these exclusions constitutes a noncompliance with Section 1 of Ordinance No. 22128 which states that the Franchisee is subject to the following provisions of the San Jose Municipal Code:

*"The grantee shall at all times maintain accurate and complete accounts of all revenue and income arising out of its operations under said franchise or franchise renewal. Grantee's books, accounts, and records shall at all times be open to inspection and examination by authorized officers, agents and employees of the city, and shall be kept in such form as to enable such authorized officers, agents and employees to ascertain the amounts of money due the city and to determine such other acts as may be necessary to determine whether or not grantee is complying with the terms of said franchise..."*

In total, the Franchisee excluded \$11,900,716 in revenues and other income from its franchise fee computations from May 1988 through November 1989. These exclusions reduced the City's cable television franchise fees by \$357,000 during that same period (\$11,900,716 x 3%).

**Absent Additional Franchisee's Justification,  
The City Was Underpaid An Estimated \$175,000  
In Franchise Fees From May 1988 Through November 1989**

City Ordinance No. 22128 changed the definition of the revenue subject to franchise fees from the "Basic 24 Channel Service" to "gross revenue". The Ordinance defines "gross revenue" as *"any and all compensation in any form, directly or indirectly recovered by Grantee from any subscriber for cable television service..."* Further, the Ordinance excludes from "gross revenue" any revenue received from installation fees, line extension fees, advertising, delinquent service charges, returned check charges and taxes. We contacted personnel in the City Attorney's Office to determine whether the \$11,900,716 in revenues and other income that the Franchisee excluded from franchise fee computations was in accordance with the City Ordinance.

Personnel in the City Attorney's Office said that revenue items such as installation charges, returned check charges, late charges, and deposits appear to be excludable items and not subject to the City's franchise fee. Other items, such as purchases, might also be excludable from franchise fee computations but the Franchisee should provide more information regarding these purchased items. The same is true for revenue items such as "Capitalized XOT," "Transaction Charge," and "Video Control Center." Without more specific information, the City cannot determine if these items should be subject to the franchise fee. Finally, personnel in the City Attorney's Office stated that, absent additional Franchisee's justification, several revenue items the Franchisee excluded from its franchise fee computations appear to be "services" within the definition of the Municipal

Code. Accordingly, these revenue items should be subject to the franchise fee. These include “Total Entertainment Package,” “Additional T.V. Pak,” “T.V. Guide Magazine,” “Express Service,” “Playboy Preview,” and “Bravo Preview.” We estimate that had the Franchisee not excluded these items from its franchise fee computations from May 1988 through November 1989, the City would have received an additional \$175,000 in cable television franchise fees.

**The Franchisee Used Unauthorized Methodologies To Calculate Franchise Fees**

Section 15 of City Ordinance No. 22128 states that the Grantee shall pay a franchise fee of three percent of gross revenues. For the purpose of this section, “gross revenues” shall mean any and all compensation in any form, directly or indirectly recovered by Grantee from any subscriber for cable television service in the City of San Jose.

During our review, we noted that the franchise fee for the third quarter of 1989 decreased \$10,493 or 3.6 percent when compared to the second quarter of 1989 as is shown below.

**FRANCHISE FEES PAID TO THE CITY**

Second Quarter <u>1989</u>	Third Quarter <u>1989</u>	Increase (Decrease)
\$291,947	\$281,454	(\$10,493)

When we analyzed the method the Franchisee used to compute the third quarter payment of \$281,454, we found that it was based upon an estimate of gross revenues. This estimate was based upon a calculated ratio

of monthly income subject to the franchise fee to total monthly income for all services. This ratio was then applied to cash receipts to arrive at the estimated franchise fee base. This fee base was then multiplied by the three percent franchise fee rate to arrive at the amount of the franchise fee remitted to the City for the third quarter of 1989. This methodology is not in accordance with Section 15 of City Ordinance No. 22128, which does not authorize an estimate as the basis for the franchise fee payment.

The Franchisee uses a service bureau, First Data Resources Inc., to process their accounts receivable. The computerized accounts receivable system identifies the cash received for the various service categories. The service bureau's computer applies payments on account to the various service categories regardless of other influencing factors. Thus, using an estimate to calculate franchise fee payments is not only unauthorized, but also unnecessary because the Franchisee's cash receipts for the various service categories (excluding bad debt recoveries) can be easily identified. It should be noted that the Franchisee did not indicate that its payment to the City for the third quarter of 1989 was an estimate. It should also be noted that the Franchisee used the amount billed to its customers as the basis for its franchise fee payment to the City for the period April 1, 1988 through June 30, 1989. This methodology is also not in accordance with Ordinance No. 22128.

In our opinion, the Franchisee has never provided adequate supporting documentation for any of the franchise fee payments to the City during the period we audited. APPENDIX B is an example of the documentation the Franchisee submits to the City to support the franchise fee payment. Such

limited documentation impairs the City's ability to review the payments for propriety. Without adequate supporting documentation, the City lacks assurance that it is receiving the correct amount of franchise fees.

### **The City Only Minimally Monitors, Reviews Or Verifies Franchise Fees**

The San Jose Municipal Code provision for cable television systems states the following reporting requirements for the grantee, *"...The grantee shall prepare and furnish to the city engineer, director of finance, city auditor and city manager, at the times and in the form prescribed by said officers, or prescribed in the franchise or franchise renewal agreement, such reports with respect to its operations, affairs, transactions or property as may be reasonably necessary or appropriate to the performance of any of the rights, functions or duties of the city or any of its officers in connection with the franchise..."* (Section 15.28.530)

While the Finance Department monitors cable television franchise fees for timeliness, it only reviews the remitted franchise fee for mathematical correctness. For example, as shown in APPENDIX B, the Finance Department verifies only the mathematical accuracy of the percentage calculations. The limited documentation does not allow the City to review the payments for completeness and propriety. In fact, the Department has neither assigned the responsibility for verifying the accuracy of this franchise fee to anyone within the Department nor required the Franchisee to complete a standardized remittance form that clearly shows how the Franchisee calculated the franchise fee paid.



According to Finance Department officials, designated Department investigator/collectors review invoiced accounts and follow up on delinquent accounts. However, the Department does not have sufficient personnel to verify non-invoiced accounts, such as franchise fees, concession fees and utility user taxes. These non-invoiced accounts generate about \$70 million a year in City revenues. We noted during our review that certain City franchisees and concessionaires submit audited financial statements to the City. We also noted that other cities in the Bay Area were generally requiring cable companies to submit audited financial statements to support franchise fee payments. However, the City does not require the Franchisee to submit audited financial statements to show in detail the gross revenues.

Finally, we noted that while Ordinance 22128 requires the Franchisee to provide reports to various City Departments, the City has no formal procedures to ensure that departments are aware of their responsibilities to:

- maintain reports;
- verify Franchisee compliance; or
- monitor Franchisee performance.

For example, Section 11 of Ordinance 22128 requires the Franchisee to maintain, on its premises, an accurate set of maps showing all cable television equipment installed in the street, alleys and public places of the City. This same section requires the Franchisee to furnish the City with copies of cable locator books as they are periodically revised. However, according to personnel in the Public Works Department, these requirements are unnecessary because state and federal law already require all contractors who perform underground work to contact a national clearinghouse called Underground Services Alert. This clearinghouse keeps up-to-date records of

all work done underground. Personnel in the Public Works Department said they neither have nor want the locator books the Ordinance requires.

Another example of interdepartmental miscommunication has to do with Risk Management. Specifically, we noted that the Franchisee had provided Risk Management with proof of insurance coverage. However, according to Risk Management staff, they were never notified that the Franchisee was required to provide proof of insurance.

## **CONCLUSION**

Current City of San Jose cable television Franchisee reporting procedures and City administrative practices expose the City to the risk of not receiving all of the cable television franchise fees to which it is entitled. Accordingly, the Franchisee needs to provide the City with additional documentation to support the franchise fees that are paid to the City. In addition, the City's ordinance prescribing the revenues that are subject to cable television franchise fees needs to be clarified to the Franchisee. Further, the Administration needs to notify various City Departments of their responsibilities regarding the City's cable television franchise. Finally, the City needs to subject submitted cable television franchise fees to additional administrative reviews.

## **RECOMMENDATIONS**

We recommend that the Finance Department:

### **Recommendation #1:**

Require the Franchisee to provide written documentation as to the composition of the revenues and income excluded from its franchise fee computations. (Priority 2)

### **Recommendation #2:**

Require the Franchisee to provide explanations for all revenue and income excluded from franchise fee computations. (Priority 2)

### **Recommendation #3:**

Require the Franchisee to submit audited financial statements to support the franchise fee payments made to the City. (Priority 2)

**Recommendation #4:**

Require the Franchisee to identify the composition of the gross subscriber revenues used and not used in the calculation of the franchise fees. (Priority 2)

**Recommendation #5:**

Develop a standardized form for the Franchisee to file that clearly shows how the franchise fee payment was derived. (Priority 2)

**Recommendation #6:**

Assign an investigator/collector to periodically review cable television franchise fees for propriety. (Priority 2)

**Recommendation #7:**

Pursue collection of any franchise fees that the City determines the Franchisee should have paid to the City but did not. (Priority 1)

We also recommend that the City Manager:

**Recommendation #8:**

Request the City Attorney to review for propriety the Franchisee's justifications for excluding revenue and income from franchise fee computations. (Priority 1)

**Recommendation #9:**

Notify appropriate City Departments as to their responsibilities in monitoring the provisions of Ordinance 22128. (Priority 3)

## FINDING II

### **THE BUDGET OFFICE NEEDS TO IMPROVE THE ACCURACY OF ITS ESTIMATED CABLE TELEVISION FRANCHISE FEES**

Each year the Budget Office prepares an estimate of the next fiscal year's cable television franchise fees. Both the City Council and the Administration rely on these revenue estimates when making budgetary decisions. Accordingly, it is essential that the Budget Office's estimates of cable television franchise fees and other revenues be as accurate as possible. However, our review revealed that the Budget Office has consistently underestimated cable television franchise fees in its budget reports. For example, in 1987-88, the Budget Office underestimated cable television franchise fees by more than \$500,000, or nearly 50 percent of actual revenues. As a result, the City Council and the Administration are making budgetary decisions based upon overly conservative cable television franchise fee estimates. In addition, the Administration is depriving itself of an important revenue control technique by using estimates that cannot be used to highlight unusual variances between estimated and actual revenues.

#### **The Budget Office's Revenue Estimating Process**

As part of the City's accrued budget process, the Budget Office prepares an estimate of the revenues for the next fiscal year's cable television franchise. We interviewed personnel in the Budget Office to determine the methodology used for estimating the franchise revenues. Our objectives were to determine:

- the accuracy of the Office's cable television franchise fee estimates;
- the assumptions the Office uses to establish the estimate of cable television franchise fees; and
- the reasonableness of the explanations regarding variances between cable television franchise fee estimates and actual results.

According to Budget Office personnel, the cable television franchise fee estimating methodology has a built-in conservative bias. In other words, the Budget Office projections are kept low to minimize the repercussions of overestimating revenues in a governmental environment. Budget Office personnel said that revenue estimates are made as early as April each year in order to have the budget ready by the end of the fiscal year. These revenue estimates are based on historical information with some allowances for increases made based upon conversations the Office has with the Franchisee. Since cable television franchise fees are a relatively small percent of the total estimated revenues for the City, the Budget Office does not spend much time estimating these fees or monitoring them throughout the year.

### **The Importance Of Accurate Revenue Estimates In The Budget Process**

Both the City Council and the Administration rely on the Budget Office's estimate of revenues when making budgetary decisions. Accordingly, it is essential that the Budget Office's estimates of cable franchise fees and other revenues be as accurate as possible.

Budgeting is an essential element of the financial planning, control and evaluation process of governments. The annual budget authorizes and

provides the basis for control of financial operations during the fiscal year. The development of estimates of revenues and expenditures is the first phase of the budget process. These estimates are the foundation of the budget and the final budget document.

According to the October 1989 “Internal Auditing Alert,” a budget can only be an effective means of measuring performance when:

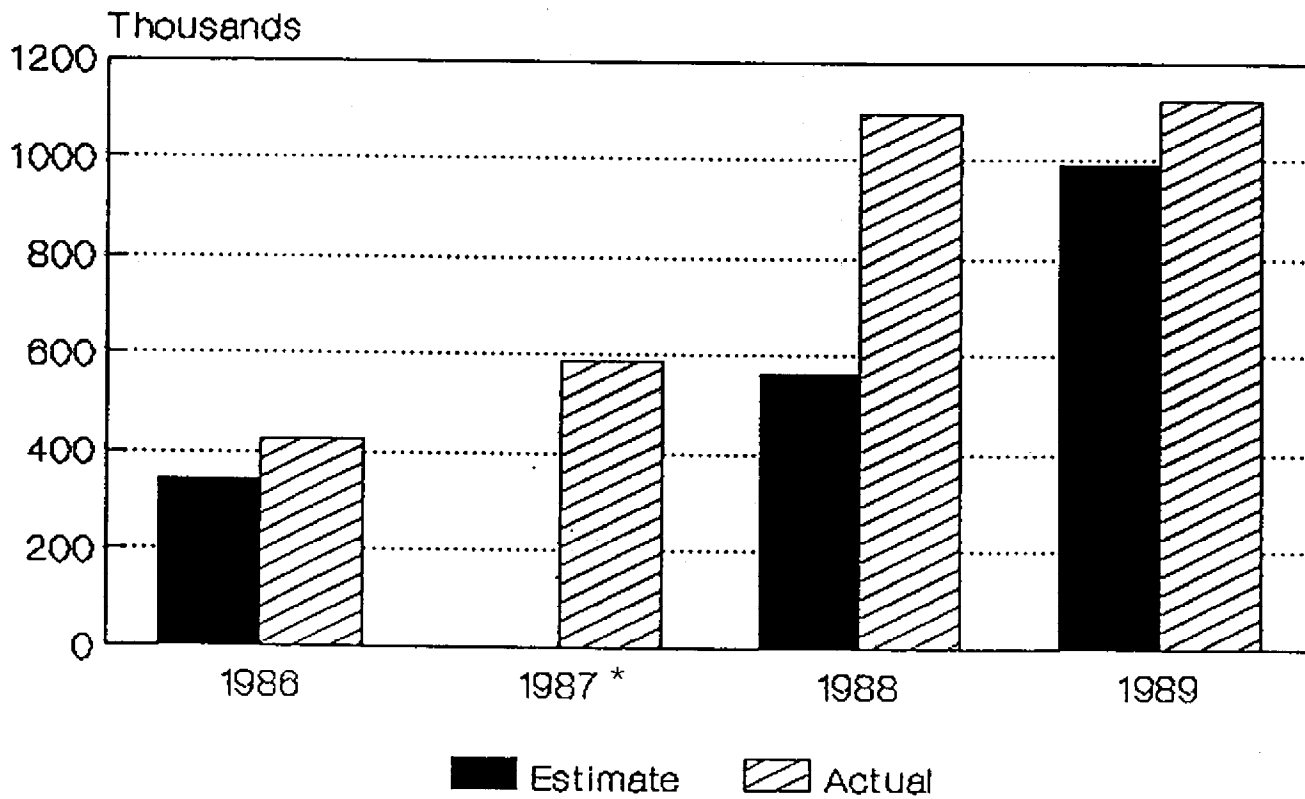
- revenues and expenditures estimates are constructed from planned estimates rather than from guesses on the basis of prior performance; and
- revenues and expenditures are the direct result of careful planning.

**The Budget Office Has Consistently Underestimated Cable Television Franchise Fees**

Our review revealed that the Budget Office has consistently underestimated cable television franchise fees in its budget preparation. As TABLE IV shows, revenue estimates for the cable television franchise have been lower than actual revenues received for three of the past four years.



**TABLE IV**  
**COMPARISON OF ESTIMATED TO ACTUAL**  
**CABLE TELEVISION FRANCHISE FEES FOR**  
**1985-86, 1987-88, AND 1988-89**



\* 1987 estimates not shown on City report.

It should be noted that the Finance Department Revenue Status Reports do not show an estimate of cable television franchise fees for 1986-87. Thus, estimated to actual cable television franchise fees for 1986-87 are not shown in TABLE IV. However, for the three years shown, actual franchise fees significantly exceeded estimated fees. This was most notably the case in 1987-88 when cable television franchise fees were underestimated by more than \$500,000 or nearly 50 percent of actual revenues. Investigation of consistent budget deviations, either favorable or unfavorable, may assist in determining faulty budget preparation or other problems.

### **The Consequences Of Overly Conservative Revenue Estimates**

Overly conservative revenue estimates cause two primary problems for the City Council and the Administration. The first problem has to do with the City Council's role in the City's annual budget process. Specifically, the City Council frequently has to make difficult budgetary decisions because of limited City revenues and multiple unfunded, competing City needs. This is especially true during times of revenue shortfalls or uncontrollable expenditure demands. Accordingly, overly conservative revenue estimates deprive the City Council of the option to appropriate City funds for deserving activities or purposes that fall outside of the City Council's budgetary priorities for a given level of available funds.

Another problem with using overly conservative revenue estimates for budgeting purposes is that it deprives the Administration of an important means of monitoring subsequent revenue collections. Specifically, the more

accurate and reliable the revenue estimates in the budget, the more likely variances from those estimates will receive administrative attention and follow-up. Thus, by improving the reliability of its cable television franchise fee estimates, the Administration would be more inclined to investigate unusual variances from those estimates. For example, as was noted earlier, in 1987-88, cable television franchise fees were underestimated more than \$500,000 or nearly 50 percent. In this case, the Franchisee could have underpaid the City \$500,000 without arousing administrative curiosity or concern. In addition, the City Council might have opted to fund additional activities or projects in 1987-88, had it anticipated that General Fund revenues would be \$500,000 more that year.

In our opinion, the Budget Office should attempt to estimate cable television franchise fees more accurately when preparing budget documents. This can be accomplished by not only analyzing historical trends and obtaining estimates from the Franchisee but also by anticipating unusual changes. For example, Section 15 of Ordinance 22128 allows the City to charge, effective January 1, 1991, a franchise fee of up to five percent of gross revenues during the remainder of the term of this franchise renewal. As a result of this franchise fee rate increase from three percent to five percent, City revenues from its cable television franchise should increase nearly \$1 million per year beginning in 1991. Accordingly, the Budget Office should take into account the provisions of Ordinance 22128 when preparing its estimate of franchise fees for 1990-91 and fiscal years thereafter.

## **CONCLUSION**

The Budget Office has consistently underestimated cable television franchise fees in the budget documents it prepares. As a result, the City Council may have been denied the opportunity to appropriate funds for worthwhile City activities or programs. In addition, the Administration has deprived itself of an important revenue control technique that would highlight revenue fluctuation and instigate administrative inquiry.

The City needs to improve estimation of revenues from Heritage Cablevision, Inc.

## **RECOMMENDATIONS**

We recommend that the Budget Office:

### **Recommendation #10:**

Take into account factors, other than historical trends, when estimating cable television franchise fees. Such factors should include written estimates of revenues from the cable television Franchisee and City Ordinance prescribed franchise rate increases. (Priority 2)

### **Recommendation #11:**

Investigate significant variances from estimated franchise fees.  
(Priority 2)

## **OTHER PERTINENT INFORMATION**

### **Customer Complaints**

In response to a request from City Council, we reviewed customer complaint procedures at Heritage Cablevision, Inc. We tested a sample of complaints and determined that problems were resolved on an average of 6.23 days. Our sample included five complaints which took over ten days and involved major repairs such as cable retrenching, sidewalk repair, or rewiring. The major repairs took from 11 days to 57 days to resolve. The average response time, excluding these five major repair complaints was 3.06 days. We also interviewed a sample of customers who filed formal complaints during 1989 to determine whether or not they were satisfied with Heritage's response to their concerns. Of the 22 customers we contacted, 16 or 73 percent were satisfied with the response. The remaining 6 or 27 percent have complaints against Heritage. Of the six outstanding complaints, four are related to reception problems and two involve complaints about cable trenching.

### **Complaint Procedures At Heritage Cablevision**

San Jose City Ordinance 22128 details customer service requirements. Accordingly, Heritage has customer service procedures for handling complaints. When a customer calls to complain about reception problems, a customer service representative identifies the customer's service area and monitors a television screen. Once the service representative is able to identify the source of the problem, a Service Request Order (SRO) is

completed and routed to dispatch. Dispatch assigns the SRO to the appropriate manager and “flags” the customer’s computer file. “Flagged” files are sorted, printed, and monitored by customer service. It is the manager’s responsibility to track the SROs and see that they are cleared from the computer. Often, Heritage is able to anticipate reception problems when they are beyond their control. For example, PG&E notifies Heritage if they will be performing work that may affect Heritage’s service. Also, certain weather conditions, such as sun spots, will affect reception. By anticipating such problems, Heritage is able to better respond to the customer’s concerns.

When Heritage receives other complaints such as workmanship, billing, or claims for damages, Heritage’s customer service department fills out a pre-numbered three-part complaint form. Customer service then inputs this information into the computer by customer name and prints out a list of all outstanding complaints. Customer service assigns responsibility to a manager according to the type of complaint and checks the status weekly until the manager returns the complaint form with a description of the disposition.

Other complaints or comments may come from the Telemarketing Department at the corporate office during telemarketing campaigns. When Telemarketing agents receive negative comments, they send a Customer Service Referral Request to the San Jose office for follow-up. Heritage initiates these complaints, not the customer.

### **Customer Satisfaction With Heritage's Complaint Response**

We selected a sample of 39 complaints from the closed file at Heritage and were able to interview 22 customers. Of the 22 we contacted, 16 (73 percent) were satisfied with Heritage's response and six (27 percent) were not. Of the six customers with outstanding complaints, four were dissatisfied with their reception. The breakdown of complaints is as follows:

25.0%	Workmanship/Damage
25.0%	Scheduling of service
22.5%	Equipment/Reception
15.0%	Price/payment
7.5%	Complaints against contractor
5.0%	Personnel

### **A COMPARISON OF CABLE PRICES IN CALIFORNIA**

Cable television pricing consists of the cost for Basic Service plus extra charges for additional outlets, Pay-per-view programs, and Premium Channels such as HBO, Showtime and Cinemax. The cost of basic cable service in San Jose is currently \$20.95 for 50 channels for an average cost per channel of \$.42. The premium charges in San Jose are \$9.95 each for HBO, Showtime, Cinemax and The Movie Channel, and \$9.50 for Disney.

We contacted 20 cable providers in the Northern California region to determine the cost of basic cable service. The monthly fee of other providers ranged from \$15.00 to \$19.00 and the cost per channel ranged from \$0.28 to \$0.78. The average cost of Basic Service is \$17.30 per month or \$0.54 per channel. The number of stations offered as part of the Basic

Service package ranged from 23 to 60. We then ranked Heritage against the other cable providers. TABLE V summarizes the results of our survey of cable television costs in the Northern California region.

**TABLE V**

**HERITAGE CABLEVISION  
PRICE COMPARISON OF OTHER  
NORTHERN CALIFORNIA CITIES**

	<u>City</u>	<u>Cable Company</u>	<u>Cost of Basic Service</u>	<u>Rank</u>	<u>Number of Channels</u>	<u>Rank</u>	<u>Average Cost Per Channels</u>	<u>Rank</u>
1	Alameda	United	\$17.80	17	52	2	\$0.34	2
2	Cupertino	United	16.95	10	45	4	0.38	3
3	Foster City	United	17.71	13	30	13	0.59	15
4	Hayward	United	16.95	9	60	1	0.28	1
5	Santa Clara	Hearst	16.50	5	23	20	0.72	20
6	Los Gatos	Hearst	17.00	11	27	18	0.63	18
7	San Francisco	Viacom	19.00	20	32	7	0.59	16
8	Antioch	Viacom	16.35	3	34	6	0.48	6
9	Belmont	TCI	17.75	16	31	9	0.57	11
10	Brisbane	TCI	17.75	14	31	10	0.57	12
11	Castro Valley	Viacom	16.75	7	29	16	0.58	13
12	Concord	Conc.Cbl	18.30	18	30	14	0.61	17
13	Fremont	TCI	17.75	15	26	19	0.68	19
14	Half Moon Bay	Weststar	16.95	8	32	8	0.53	9
15	Marin County	Viacom	17.00	12	31	11	0.55	10
16	Milpitas	Hearst	16.50	4	28	17	0.59	14
17	Monterey	TCI	16.70	6	23	21	0.73	21
18	Pacifica	TCI	18.55	19	39	5	0.48	5
19	Petaluma	Viacom	15.00	1	31	12	0.48	7
20	Pinole	Viacom	15.00	2	30	15	0.50	8
<b>21</b>	<b>San Jose</b>	<b>Heritage</b>	<b>20.95</b>	<b>21</b>	<b>50</b>	<b>3</b>	<b>0.42</b>	<b>4</b>
	AVERAGES		17.30		34		0.54	